Audit Report

State Department of Assessments and Taxation

August 2007

OFFICE OF LEGISLATIVE AUDITS
DEPARTMENT OF LEGISLATIVE SERVICES
MARYLAND GENERAL ASSEMBLY

- This report and any related follow-up correspondence are available to the public through the Office of Legislative Audits at 301 West Preston Street, Room 1202, Baltimore, Maryland 21201. The Office may be contacted by telephone at 410-946-5900, 301-970-5900, or 1-877-486-9964.

- Electronic copies of our audit reports can be viewed or downloaded from our website at http://www.ola.state.md.us.

- Alternate formats may be requested through the Maryland Relay Service at 1-800-735-2258.

- The Department of Legislative Services – Office of the Executive Director, 90 State Circle, Annapolis, Maryland 21401 can also assist you in obtaining copies of our reports and related correspondence. The Department may be contacted by telephone at 410-946-5400 or 301-970-5400.

DEPARTMENT OF LEGISLATIVE SERVICES
OFFICE OF LEGISLATIVE AUDITS
MARYLAND GENERAL ASSEMBLY

Karl S. Aro
Executive Director

Bruce A. Myers, CPA
Legislative Auditor

August 24, 2007

Delegate Steven J. DeBoy, Sr., Co-Chair, Joint Audit Committee
Senator Nathaniel J. McFadden, Co-Chair, Joint Audit Committee
Members of Joint Audit Committee
Annapolis, Maryland

Ladies and Gentlemen:

We have audited the State Department of Assessments and Taxation (DAT) for the period beginning October 16, 2003 and ending January 31, 2007.

Our audit disclosed that DAT did not adequately pursue the collection of fees and penalties from foreign corporations that had forfeited their corporate charters but appeared to be conducting business in Maryland, in violation of State law. DAT should ensure that property owners listed in its residential property records only receive the Homestead Tax Credit for their principal residences.

DAT had not adequately investigated the reasons why, in eight jurisdictions, the ratio of assessment to sales prices for commercial properties sold in fiscal year 2006 was much lower than the remaining jurisdictions. Finally, DAT had certain internal control and record keeping deficiencies relating to cash receipts, accounts receivable, information systems security, and payroll.

Respectfully submitted,

Bruce A. Myers, CPA
Legislative Auditor

Table of Contents

* **Denotes item repeated in full or part from preceding audit report**

Executive Summary

Legislative Audit Report on State Department of Assessments and Taxation (DAT)
August 2007

- **DAT did not take appropriate action to pursue over 1,000 foreign (non-Maryland) corporations that were potentially conducting business in Maryland which would require the corporations to file annual reports, personal property tax returns, and remit the related fees.**

  DAT should take appropriate action to obtain any amounts and returns identified as due by sending annual notices to all forfeited foreign corporations identified from its automated matching procedures as potentially conducting business in Maryland. DAT should also take action against forfeited foreign corporations that do not respond to its notices.

- **DAT should ensure that each property owner listed in its residential property records only receives the homestead tax credit for their principal residence.**

  DAT should implement its plan to require property owners to apply for the tax credits to help ensure that the credits are properly received.

- **Certain variances in the ratio of assessed value to sales price for commercial properties were not adequately investigated by DAT.**

  DAT should investigate and document the reasons for significant variances and take appropriate action to ensure all local assessment offices meet industry standards to the extent possible.

- **DAT did not verify that amounts paid to local jurisdictions for redeemed tax credits were proper and it did not ensure that all tax credits were recovered for homes that had been sold.**

  DAT should research differences identified in its automated matches of tax credits approved for issuance to the tax credits redeemed by local jurisdictions and recover erroneous credits identified. DAT should also establish procedures to ensure that local jurisdictions recover all homeowners' tax credits for residential properties that transferred ownership.

- **Additional internal control and recordkeeping deficiencies were noted with respect to cash receipts, accounts receivable, information systems security and payroll.**

  DAT should take the recommended actions to improve controls and record keeping deficiencies in these areas.

Background Information

Agency Responsibilities

The State Department of Assessments and Taxation (DAT) is responsible for administering the State's real and personal property tax laws as well as for various functions applicable to corporations (for example, issuing corporate charters and collecting certain taxes, such as gross receipts tax). DAT also administers programs that provide property tax credits primarily to homeowners and renters who meet the related eligibility requirements (such as gross income limitations). DAT's headquarters is located in Baltimore City. DAT operates assessments and taxation offices in each of the State's 24 local jurisdictions. According to the State's records, during fiscal year 2006, DAT's operating expenditures totaled approximately $96.2 million.

Current Status of Findings From Preceding Audit Report

Our audit included a review to determine the current status of the seven findings contained in our preceding audit report dated August 10, 2004. We determined that DAT satisfactorily addressed six of these findings. The remaining finding is repeated in this report.

Findings and Recommendations

Corporate Filing Fees

Finding 1
DAT did not take appropriate action to pursue approximately 1,100 foreign (non-Maryland) corporations that were potentially conducting business in Maryland but had failed to file required annual reports and personal property tax returns, and potentially failed to remit the related fees.

Analysis
DAT did not take appropriate action to pursue foreign (domiciled outside Maryland) corporations conducting business in Maryland even though the corporations had previously forfeited their rights to do business in the State due to nonfilings. As provided by State law, DAT places corporations in forfeited status when they fail to file at least one annual report and personal property return and remit the related fees. DAT performed automated matches to detect foreign corporations potentially conducting business in Maryland. DAT initially performed this match in 2003, and also in fiscal years 2005 and 2006. As of April 2007, the 2006 match was still in progress since DAT had not mailed first notices to all corporations identified in that match. Our review of DAT's actions to pursue forfeited foreign corporations identified as continuing to conduct business in the State disclosed the following conditions:

- The 2005 match identified 1,146 forfeited foreign corporations that were apparently conducting business in Maryland because the corporations either had active sales tax accounts (574 corporations) or had received a State vendor payment (572 corporations), according to the Comptroller's records for fiscal year 2005. While DAT mailed notices requesting information regarding their operations in Maryland to 600 of the aforementioned 1,146 foreign corporations, it took no action regarding the remaining 546 forfeited foreign corporations that were potentially conducting business in Maryland. In response to our preceding audit report, DAT stated that it would follow up on all corporations identified in these matches. Furthermore, DAT took no further action to determine if the 600 corporations were conducting business in Maryland if they failed to respond to two notices. Specifically, no follow-up was performed on the 387 foreign corporations that failed to respond to two DAT notices, although DAT had found that 152 of the corporations who had responded were qualified corporations that should have filed. An official of the State Comptroller's Office advised us that corporations who fail to respond to DAT's requests for information should be referred to the

Department of Budget and Management's Central Collection Unit. The Unit could then intercept any delinquent property tax filing fees and penalties from the Office of the Comptroller's vendor payments to the corporations. An Assistant Attorney General assigned to the Department of Budget and Management also advised us that corporations who do not respond to DAT notices could be referred to the Unit. However, this conflicted with advice received from the Assistant Attorney General assigned to DAT who advised that the corporations should not be referred to the Central Collection Unit.

- Numerous foreign forfeited corporations identified during our preceding audit that were potentially conducting business in Maryland during fiscal year 2003 were also identified in DAT's automated matches conducted for calendar years 2005 and 2006. Specifically, our review of 1,108 foreign forfeited corporations identified during our prior audit disclosed that, during fiscal years 2005 and 2006, 262 of these corporations had active sales tax accounts and an additional 84 of these corporations had received State vendor payments totaling approximately $7.5 million during fiscal years 2005 and 2006. If all 346 of these forfeited corporations were required to file with DAT, we estimated that filing fees and penalties applicable to these corporations could total as much as $1.1 million.

We acknowledge that some of the corporations identified by the matches may not actually be conducting business in Maryland. Additionally, certain entities, such as non-stock corporations, are legally exempt from paying the annual filing fee. Furthermore, we were advised by DAT management that it was concerned about the cost/benefit of pursuing the match results. However, we continue to believe, particularly based on the results of our comparison above and DAT follow up of the 2005 match, that procedures should be established to help ensure that foreign corporations are in compliance with the law and are paying all amounts due.

Recommendation 1
We recommend that DAT take appropriate action to obtain any reports, returns and amounts identified as due. Specifically, we recommend that DAT send annual notices to all forfeited foreign corporations identified from its automated matching procedures as potentially conducting business in Maryland. We further recommend that DAT take action against forfeited foreign corporations that do not respond to its notices. We also recommend that DAT obtain legal clarification regarding the actions, such as referring the corporations to the Central Collection Unit, which can be taken when corporations do not respond to DAT notices.

Homestead Tax Credit

Finding 2
DAT should ensure the eligibility of properties, which allows owners to receive the homestead property tax credits.

Analysis
DAT should implement procedures to ensure that owners of multiple residential properties only receive the homestead tax credit for their principal residence. State law provides that a property must be the principal residence of the owner in order for the owner to receive the homestead credit. The homestead credit limits the annual increase in the owner's State property tax bill due to assessment increases to 10 percent and the property tax bill for each local jurisdiction to 10 percent or less as determined by each jurisdiction. The table below summarizes the homestead credits issued during the 2006/2007 tax year according to DAT records:

Summary of Homestead Tax Credits – 2006/2007 Tax Year				
Credit Type	Residential Properties	Properties Receiving Homestead Credits	Decrease in Property Assessments Due to Homestead Credits	Estimated Value of Homestead Credits
State	1,359,598	957,189	$ 34,059,310,241	$ 38,146,427
County	1,359,598	1,157,642	$ 55,446,066,330	$ 500,597,285

Source: DAT records

Legislation enacted during the 2007 session of the General Assembly requires all homeowners to file applications with DAT to qualify for the credit. However, the legislation generally does not require the use of applications until 2012. We were advised that the application process should help prevent homeowners from receiving the credit on multiple properties. Although DAT is not generally required to obtain applications from homeowners for the homestead credit until 2012, we were advised that DAT plans to require applications for all properties that are reassessed beginning in December 2007.

Adoption of a new process to help prevent improper credits is needed because the existing processes to verify eligibility have not been comprehensive. Generally, residential properties are identified as such during settlement without performing certain subsequent verification procedures. For example, DAT did not review its own records for property owners that received the credit on multiple properties. We noted that one county's finance office recently identified approximately 1,000 instances of property owners who may have received credits on multiple properties within the county. As of May 5, 2007, the office had investigated 103 of the properties and identified 63 properties (61%) that should not have received the credit. During fiscal year 2007, the improperly awarded credits resulted in lost revenue to the county of approximately $34,000. Furthermore, our test of 25 rental properties in Maryland advertised on the internet on March 13, 2007, disclosed that 15 properties were classified in DAT's real property records as the owner's principal residence and were thus eligible for the credit. We provided DAT with a listing of the 15 properties for investigation. As of June 29, 2007, DAT had removed the principal residence designation from 8 of these properties.

Recommendation 2
We recommend that DAT implement its plan to require property owners to apply for the tax credits to help ensure that the credits are properly received.

Real Property Assessments

Finding 3
DAT did not adequately investigate and document the reasons for certain variances between the assessed value and sales price of commercial properties.

Analysis
DAT did not adequately investigate and document the reasons for variances between the assessed value and sales price of commercial properties in certain jurisdictions. Specifically, compared to other jurisdictions, DAT's 2006 Assessment Ratios Survey Report disclosed that assessed values of commercial properties in eight jurisdictions (with 10 or more sales during fiscal year 2006) were much lower than their sale prices.

For the 402 sales of commercial properties (totaling $559 million) occurring in these eight jurisdictions during fiscal year 2006, the properties were, on a weighted average basis, assessed at 69 percent of their sales price while the comparable ratio for the remaining jurisdictions was 88 percent. The weighted averages for each of the eight jurisdictions ranged from 52 percent to 73 percent. However, the Report did not adequately explain the apparent under-assessment of commercial properties in the eight jurisdictions. The ratio report, which DAT is required to produce by State law, compared sales prices of real property that sold during fiscal year 2006 to the assessed values of properties as of January 1, 2006.

In the Report, DAT attributed the low assessment value to sales price ratios to rapidly escalating prices and a limited number of sales of commercial properties.

However, there was no indication that the market situations and sales activities were unique to these jurisdictions. Other jurisdictions' ratios were generally within industry standards, indicating that the assessments of commercial properties in the State's other jurisdictions were closer to their market values.

Standards issued by the International Association of Assessing Officers, which DAT has adopted, call for properties to be assessed at least 90 percent of their market values. As previously noted, the ratio for the other 16 jurisdictions, on a weighted basis (88 percent) is close to this standard. However, because of the lower assessments to sale prices ratio of the eight jurisdictions (69 percent), the overall statewide ratio was 84 percent.

The assessable base of all commercial property within these eight jurisdictions represented approximately $36 billion (35 percent) of the $102 billion assessable base for commercial property in Maryland, according to DAT's records. Annual local property tax revenue from the commercial properties in these jurisdictions totals approximately $400 million while annual State property tax revenue from the properties exceeds $40 million. Therefore, any significant under-assessment of commercial properties could substantially reduce property tax revenues received by local governments and the State.

Recommendation 3
We recommend that DAT investigate and document the reasons for significant variances between assessed values and sales prices of commercial properties and take appropriate action to ensure all local offices meet industry standards to the extent possible.

Monitoring of Homeowners' Tax Credits

Finding 4
DAT did not verify that amounts paid to local jurisdictions for redeemed homeowners' tax credits were proper and did not ensure that all credits were recovered for homes that were sold.

Analysis
DAT did not verify the propriety of amounts paid to local jurisdictions for homeowners' tax credits redeemed. After DAT has processed the tax credit application and approved the homeowners' credits, it notified the local jurisdictions that the credits were approved. Furthermore, after the credits had been redeemed by taxpayers (either by the local jurisdiction recording a credit on the property tax bill or issuing a check to the taxpayer), DAT reimbursed the local

jurisdictions for the credits. Although DAT's computer system performed a monthly match of the tax credits that it had approved for issuance to the tax credits redeemed by local jurisdictions, no employee researched and resolved differences identified by this match. For example, the monthly match for one jurisdiction for the month of September 2006 identified reimbursements totaling approximately $79,000 that did not agree to DAT's records of credits authorized. As a result of these conditions, DAT may not detect erroneous reimbursement amounts paid to the local jurisdictions.

In addition, DAT did not compare its records of properties sold to reports of tax credits recovered on sold properties which were prepared by the local jurisdictions. Rather, DAT relied on local jurisdictions to identify and recover all such tax credits from taxpayers. Consequently, DAT lacked assurance that all homeowners' tax credits for properties transferred to new ownership were recovered and reimbursed to DAT as required by State law. According to DAT's records, during fiscal year 2006, collections from the recapture of homeowners' tax credits related to applicants who sold their residential properties totaled approximately $304,000.

Homeowners are eligible for a homeowners' tax credit based on meeting certain income eligibility requirements. If the properties are subsequently transferred to new owners, State law provides for the tax credits to be recaptured. According to DAT records, homeowners' tax credits totaled approximately $41 million during fiscal year 2006.

Recommendation 4

We recommend that DAT employees research differences identified in monthly automated matches of tax credits and recover erroneous reimbursements identified. We also recommend that DAT establish procedures to ensure that local jurisdictions recover all homeowners' tax credits for residential properties that transferred ownership during the tax year applicable to the credit and remit the recovered credits to DAT.

Cash Receipts

Finding 5
Cash receipts were not adequately controlled to ensure that all collections initially recorded were subsequently deposited.

Analysis
DAT did not establish adequate internal controls over cash and check collections received at DAT's headquarters office. Collections, such as personal property tax filing fees, totaled approximately $35.6 million (cash collections of approximately $1.3 million and check collections of approximately $34.3 million) during fiscal year 2006. Cash collections were initially recorded on a cash register system and subsequently posted to an automated system while check collections were recorded directly to the automated system. Specifically, we noted the following conditions:

- Duties relating to cash processed through DAT's cash register system were not properly segregated. Specifically, five employees could operate the cash register system, process voided transactions, and perform daily closeout procedures. Furthermore, independent reviews of voided receipt transactions were not performed to verify the propriety of such transactions. Similar conditions were commented upon in our preceding audit report.

- DAT did not perform independent verifications to ensure that all check collections recorded in its automated system were deposited. Rather, the report used to verify that collections were deposited was prepared by an employee with access to the collections. A similar condition was commented upon in our two preceding audit reports.

- Four employees who worked as cashiers could also record non-cash credit adjustments to business accounts in DAT's automated system without approval. Consequently, these employees could misappropriate collections without detection.

- Another employee, who had access to collections, could process non-cash credits on DAT's automated system without approval and also reconciled the system to the State's accounting records.

Recommendation 5
We again recommend that the responsibilities for conducting register closeout procedures and reviewing the propriety of voided transactions be

performed by an employee independent of the cash receipts function. In addition, we again recommend that an employee independent of the cash receipts function verify that all recorded collections have been deposited. We also recommend that employees with access to collections not be permitted to record non-cash credit adjustments to business accounts. Finally, we recommend that employees responsible for reconciling DAT's records to the State's records not have access to cash receipts. We advised DAT on accomplishing the necessary separation of duties using existing personnel.

Accounts Receivable

Finding 6
Accounts receivable records were not maintained for recoveries of excess tax credits.

Analysis
DAT's Taxpayer Services Division lacked accounts receivable records for recoveries of excess homeowners' and renters' tax credits identified from the comparison of income reported on credit applications to income per the State Comptroller's income tax records. These tax credits are granted to set limits on the amounts of property taxes due from taxpayers based upon their income. In this regard, even though tax credits are granted based on a copy of a federal tax return that is submitted with the individual's tax credit application, DAT also subsequently compares that income information with State tax information received from the State Comptroller.

DAT maintained records that were used to monitor excess tax credits (including the recipient's name and the total tax credit to be recovered), but the records did not identify unpaid amounts currently due or the account billing history. As of May 10, 2007, approximately 8,000 individual credit recipients were listed in DAT's automated system. As a result, we could not readily determine the accounts receivable balance, whether routine billings were issued, or whether delinquent accounts were referred for collection to CCU as required. According to DAT's records, collections of excess tax credits resulting from verification of recipient reported income totaled approximately $349,000 during fiscal year 2006.

Recommendation 6
We recommend that DAT establish and maintain formal accounts receivable records for all recoveries of excess tax credits identified. We also

recommend that these records be maintained accurately and on a current basis, and that they be used to monitor the payment status of related billings.

Information Systems Security and Control

Background
DAT operates several critical computer applications on its internal network and on the Comptroller of the Treasury's Annapolis Data Center (ADC). These applications include property assessment databases and property tax credit databases. DAT also operates a statewide network that connects its local offices and DAT headquarters internal network. DAT's statewide network offers users access to various information technology services including ADC mainframe computer-based applications, a database management system, network services, email services, and Internet access. DAT's network includes firewalls as well as an intrusion detection/prevention system device.

Finding 7
Controls over a critical firewall and the intrusion detection/prevention system need improvement.

Analysis:
Controls over a critical firewall and the intrusion detection/prevention system (IDPS) need improvement. Specifically, we noted the following conditions:

- The firewall protecting the network from the Internet was a software firewall operating on a server. The firewall software vendor discontinued support for the installed firewall software effective February 28, 2003. As a result, the firewall software was in use for a period of over four years during which time patches, fixes, and general software updates did not exist.

- The operating system on the server hosting the firewall had not been updated to fix several security concerns. Specifically, the operating system had not been updated since September 2005, and a check on a national vulnerability database disclosed that 11 software vulnerabilities were identified for this operating system software since September 2005.

- Password and account controls on the server hosting the firewall did not meet the requirements set by the Department of Budget and Management's *Information Technology Security Policy and Standards.* For example, the minimum password length was set to "0" and there was no lockout provision for failed logon attempts.

- While we were advised that the firewall's event log information was reviewed weekly, no documentation existed to substantiate that these periodic reviews of the firewall logs were performed. In addition, the firewall was not set to send email alerts to network personnel to alert them of critical and emergency problems with the firewall.

- The IDPS was not configured to send alerts to network administrators advising them of serious concerns detected by the system. In addition, the IDPS logs contained incorrect source addresses of traffic analyzed because all inbound traffic source addresses were changed by DAT's firewall before the traffic reached the IDPS. As a result, this would greatly hinder any investigation into what entities were attacking DAT's network. Finally, although DAT advised us that the IDPS logs were reviewed on a daily basis, documentation did not exist to substantiate these reviews.

Recommendation 7
We recommend that DAT implement appropriate controls over the aforementioned critical firewall and IDPS. Accordingly, we made detailed recommendations to DAT which, if implemented, should provide adequate controls over these areas.

Payroll

Finding 8
The same employee could initiate and approve personnel transactions.

Analysis
DAT did not adequately control access to the automated system used to process personnel transactions (such as adding new employees and changing salaries). Specifically, one employee had two userids which, when combined, allowed the employee to initiate and approve personnel transactions without independent approvals.

The Department of Budget and Management (DBM) implemented an automated system that allowed State agencies to submit personnel data electronically for entry on the State's personnel system. We were advised by DBM that system controls prevent the same userid from both initiating personnel transactions, and submitting recorded changes to DBM. However, by obtaining two userids for an employee, DAT has circumvented this system control. DAT's payroll expenditures during fiscal year 2006 were approximately $39 million for 677 employees.

Recommendation 8
We recommend that DAT not assign employees more than one userid and that all personnel transactions are approved by supervisory personnel other that the employee who initiated the transaction.

Audit Scope, Objectives, and Methodology

We have audited the State Department of Assessments and Taxation (DAT) for the period beginning October 16, 2003 and ending January 31, 2007. This audit was conducted in accordance with generally accepted government auditing standards.

As prescribed by the State Government Article, Section 2-1221 of the Annotated Code of Maryland, the objectives of this audit were to examine DAT's financial transactions, records, and internal control, and to evaluate its compliance with applicable State laws, rules, and regulations. We also determined the current status of the findings contained in our preceding audit report.

In planning and conducting our audit, we focused on the major financial-related areas of operations based on assessments of materiality and risk. Our audit procedures included inquiries of appropriate personnel, inspections of documents and records, and observations of DAT's operations. We also tested transactions and performed other auditing procedures that we considered necessary to achieve our objectives. Data provided in this report for background or informational purposes were deemed reasonable, but were not independently verified.

DAT provides certain support services (such as payroll, invoice processing, maintenance of accounting records and related fiscal functions) to the Property Tax Assessment Appeals Board. These support services are included within the scope of our audit of DAT.

Our audit scope was limited with respect to DAT's cash transactions because the Office of the State Treasurer was unable to reconcile the State's main bank accounts during a portion of the audit period. Due to this condition, we were unable to determine, with reasonable assurance, that all DAT cash transactions prior to July 1, 2005 were accounted for and properly recorded on the related State accounting records as well as the banks' records.

DAT's management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that objectives pertaining to the reliability of financial records, effectiveness and efficiency of operations including safeguarding of assets, and compliance with applicable laws, rules, and regulations are achieved.

Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or compliance with policies and procedures may deteriorate.

Our reports are designed to assist the Maryland General Assembly in exercising its legislative oversight function and to provide constructive recommendations for improving State operations. As a result, our reports generally do not address activities we reviewed that are functioning properly.

This report includes findings relating to conditions that we consider to be significant deficiencies in the design or operation of internal control that could adversely affect DAT's ability to maintain reliable financial records, operate effectively and efficiently, and/or comply with applicable laws, rules, and regulations. Our report also includes findings regarding significant instances of noncompliance with applicable laws, rules, or regulations. Other less significant findings were communicated to DAT that did not warrant inclusion in this report.

DAT's response to our findings and recommendations is included as an appendix to this report. As prescribed in the State Government Article, Section 2-1224 of the Annotated Code of Maryland, we will advise DAT regarding the results of our review of its response.

APPENDIX

State of Maryland

DEPARTMENT OF ASSESSMENTS AND TAXATION

Office of the Director

MARTIN O'MALLEY
Governor

C. JOHN SULLIVAN, JR.
Director

WAYNE M. SKINNER
Deputy Director

August 21, 2007

Mr. Bruce A. Myers, CPA
Legislative Auditor
Department of Legislative Services
Office of Legislative Audits, Room 1202
Maryland General Assembly
301 W. Preston Street
Baltimore, MD 21201

Dear Mr. Myers:

Enclosed you will find a copy of State Department of Assessment & Taxation's (SDAT) response to the Draft Audit Report of our Department dated August, 2007.

If you have any questions or need additional information regarding the responses, please contact James P. Wallace, Associate Director of Finance and Administration, State Department of Assessments and Taxation at 410-767-1194.

Sincerely,

C. John Sullivan, Jr.
Director

Enclosure

300 West Preston Street – Room 605 – Baltimore, Maryland 21201
Phone: (410) 767-4881 – Fax: (410) 333-5873 – TTY users call Maryland Relay 1-800-735-2258
Toll Free: 1-888-246-5941 – Website: www.dat.state.md.us

Finding #1 – Corporate Filing Fees

The Department Concurs. *The Comptroller's vendor, sales tax and withholding tax will be used in finding foreign forfeited corporations doing business in the State of Maryland. Additionally, the Department will seek legal clarification on actions that the Department can take regarding those entities that do not respond to our notices.*

Finding #2 – Homestead Tax Credit

The Department Concurs*. The proper automated audit of homestead tax credits is the one codified in the new law enacted by the 2007 session of the General Assembly. Removing homestead credits for homeowners with multiple properties can only be done with name matches that are tied to individual Social Security numbers. This is why the Department played an instrumental role in supporting this Legislation which requires all homeowners wanting to retain the homestead tax credit to make a formal application to the Department and supply their Social Security numbers on that application for matching with the data records of the IRS, the Comptroller's Office and the Motor Vehicle Administration (MVA). The Department will be sending out applications to one – third of all homeowners in the State being reassessed for January 1 of 2007 and to another 175,000 transferees of residential properties each year. The Department will start removing homestead credit designations for homeowners who do not submit the new homestead application within a sixty (60) day period; the Department will promulgate by Administrative Rule. The December 31, 2012 date in the new law cited by the Auditors is an "outside" date which the Department will limit by Administrative Rule to the aged and infirmed.*

Finding #3 – Real Property Assessments

The Department Concurs. *The Department will investigate procedures in the eight identified jurisdiction and document if they are not performing to industry standards. The Department will analyze the types of sales included in the ratio study and will investigate, if any time adjustments can be determined from the marketplace.*

The Department has tried unsuccessfully, to support legislation that would have sales data through the transfer of controlling interests made available. Many sales are accomplished through this process and it is unreported. This data is critical and would greatly assist with the accuracy of valuations. Most benchmark sales are transferring outside of the deed process. It has been argued that sophisticated buyers and sellers are using the transfer of the controlling interest of the entity, rather than land records, when properties are sold. The quality of commercial assessments and the commercial ratio will continue to be negatively affected by the lack of sales data available for analysis. The Department has identified properties throughout the State which have transferred outside of land records. Without good data on all property sales, both within and outside of land records, commercial assessments will continue to suffer. This will negatively impact any ratio analysis of commercial properties.

In conclusion, a revenue change cannot be projected from an apparent over or under assessment of commercial properties. Several local jurisdictions have revenue limitations. In these jurisdictions (Anne Arundel, Montgomery, Wicomico, and Talbot Counties), a significant base change would most likely result in a tax rate change. The State property tax rate is dedicated to the annuity bond fund. Any significant change in base could result in a change in the tax rate. Local jurisdictions are responsible for the setting of their tax rates. The assessment and the tax rate together determine the property tax revenue. The Department cannot determine what tax rate the counties and towns would have set if their assessable base had been different.

Finding #4 Monitoring of Homeowners Tax Credits

The Department Concurs*. Additional training to new personnel has already taken place expanding responsibilities and making them aware of the capabilities of the automated system. The Department had designed an automated reporting system and had been performing all of these audits on recaptured tax credits and reimbursements for years.*

Finding #5 – Cash Receipts

The Department Concurs. *The supervisory level employee with access to cash and check collections in order to process adjustments (such as checks returned for insufficient funds) must have a signed authorization from one of the four senior independent Program Managers (Charter Legal, Charter Processing, Accounting and Personal Property). The Charter Processing Program Manager independently conducts random audits of the adjusted accounts to insure the appropriate other Program Manager has signed to authorize the specific adjustment transaction. Due to the volume of transactions, the processing manager conducts random audits of transactions.*

The Department will have all positions filled by September 15 and duties will be delegated out to new personnel in the Accounting Section. This should enhance internal controls and comply with segregation of duties that were recommended by the audit staff.

Finding #6 – Accounts Receivable

The Department Concurs. *The Department will take advantage of A/R system that is part of FMIS and will produce information on monthly basis for program staff.*

Finding #7 – Information Systems Security and Control

The Department Concurs. *DAT has installed a new firewall appliance which includes IPS software. All activity of the new firewall is being logged to a separate server in which DAT personnel will review daily upon completion of the project scheduled for 8-31-2007. Daily files will be addressed and signed off by OIT personnel, in addition to, e-mail alerts are being established which also will be completed by 8-31-2007.*
DAT is establishing a Firewall Security policy which will be separate from the Department's overall information systems security policy. This will be accomplished once the firewall project is completed by 8-31-2007.

DAT no longer has the previously used software housing its firewall, in which DAT-OIT acknowledges that passwords were not followed by standards due to the fact only 2 people had access to the server. Passwords and account controls have been modified to comply with standards.

Finding #8 - Payroll

The Department Concurs. *Correction has already taken place.*

AUDIT TEAM

Stephen C. Pease, CPA
Audit Manager

Stephen P. Jersey, CPA, CISA
A. Jerome Sokol, CPA
Information Systems Audit Managers

Abdullah I. Adam
Senior Auditor

Albert E. Schmidt, CPA
Information Systems Senior Auditor

Nichole M. Becker
Menachem Katz, CPA
Edward J. Welsh
Staff Auditors

Veronica A. Arze
Information Systems Staff Auditor